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BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to Implement the Commission's Procurement Incentive Framework and to Examine the Integrations of Greenhouse Gas Emissions Standards into Procurement Policies.
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Rule making R.06-04-009

CEC Docket No. D.07-OIIP-01

COMMENTS OF COVANTA ENERGY CORPORATION

ON THE MARKET ADVISORY COMMITTEE REPORT

August 6, 2007

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COMMENTS OF COVANTA ENERGY CORPORATION ON THE MARKET ADVISORY COMMITTEE REPORT

Introduction

Pursuant to the July 19, 2007 Administrative Law Judge's Ruling Requesting Comments and Legal Briefs on the Market Advisory Committee Report and Notice of En Banc Hearing, in R.06-04-009, the Order Instituting Rulemaking to Implement the Commission's Procurement Incentive Framework and to Examine the Integration of Greenhouse Gas Emissions Standards into Procurement Policies, Covanta Energy Corporation ("Covanta") respectfully submits these Comments of Covanta Energy Corporation on the Market Advisory Committee Report. Our submittal and any additional information we may submit during the pendency of your deliberations over what you will recommend to the Air Resources Board ("ARB") relative to the implementation of AB 32.

Background on Covanta Energy Corporation

Covanta currently operates over thirty Energy-from-Waste ("EfW") facilities from North America to Asia with an expanding presence in California. Covanta's core business focuses on the conversion of Municipal Solid Waste ("MSW") to energy in partnership with communities eager to address their energy and disposal needs in an environmentally responsible manner. Covanta's EfW facilities have a combined production rate of 7,800 GWh per year of renewable electricity annually. While producing this renewable electricity, Covanta recovers and recycles approximately

360,000 tons of metals from waste and processes 5% of the nation's waste stream[1]. In Stanislaus County, Covanta's facility processes approximately 800 tons of solid waste daily. It has installed capacity of approximately 22 megawatts that produces about 135,000 MWh of renewable energy annually which is sold to Pacific Gas and Electric to meet its renewable energy targets mandated by state law. The Stanislaus facility is a "zero water discharge plant" meaning the waste water produced on the site is treated and reused. Covanta's renewable technology is aiding Stanislaus County to attain a solid waste 64% recycling/diversion rate pursuant to the CIWMB's AB 939 mandates.

In addition to the Stanislaus facility, Covanta also has several other renewable biomass to energy plants located in the California communities of Burney, Westwood, Jamestown, Oroville, Mendota, and Delano. Covanta also operates four Landfill Gas to Energy facilities in Stockton, Salinas, Oxnard and Chula Vista. Across all of our California facilities, Covanta employs 210 people and produces approximately 645 GWh of renewable energy annually from its 155 MW renewable portfolio in the state (including EfW, Biomass, and Biogas). Electricity from our California renewable portfolio is sold to California Investor Owned Utilities under long-term Power Purchase Agreements.

Relevant Market Advisory Committee Finding

[1] Additional information on the company may be obtained at www.covantaholdings.com

AB 32 requires that significant sources of greenhouse gas emissions be reported to and regulated by the ARB (H&S Sec. 38505 (h) (i)). In its final report to the ARB, the Market Advisory Committee ("MAC") determined that the category of waste combustion produced about 100,000 tons of greenhouse gas in 2004. This represents less than 0.02% of the 494,300,000 tons of greenhouse gases produced in the state[2] during the same year. Based on this finding and our internal analysis, we conclude that the three EfW facilities in California, of which our Stanislaus facility is one, should be exempt from inclusion in any regulatory program to reduce Green House Gas ("GHG") emissions in the electricity sector since EfW facilities in the state produce insignificant amounts of GHG. Taken together, the disposal of MSW in our Stanislaus EfW facility results in the following benefits:

- Avoids GHG emissions that would otherwise result from landfilling MSW
- Recaptures ferrous material for recycling, and
- Generates approximately 20MW Renewable Portfolio Standard-compliant electrical power per-year

Based on the above, we argue that the Stanislaus facility does, in fact, function as a net GHG reducer.

As a matter of fact, the Kyoto protocol recognizes EfW facilities as potential net greenhouse gas reducers and permits the issuance/trading of GHG credits generated by such facilities. The recently approved UNFCCC protocol (AM0025 version 7) establishes concise methodology for qualifying EfW facilities for the production of GHG credits. The AM0025 methodology recognizes the benefit of EfW in two main categories; the elimination of methane that would otherwise result from landfilling of waste and the elimination/reduction of the need to use fossil fuels for electricity

[2] See the page 108 of the MAC report.

generation. The AM0025 methodology is designed to be flexible enough to address local grid/landfill situations in various areas in the world. The same methodology could be and should be adopted to address EfW in California. Substantial departure in California from the Kyoto protocol/international GHG rules will make it difficult to create future linkages between the California GHG program and international GHG markets[3].

Overall Policy Perspective

Industry associations of which Covanta is a member will provide perspectives on many of the specific sector-related questions that have been thoughtfully put forward by the staffs of your two commissions. We will provide comments, as necessary, during the reply phase of this proceeding on the submittals offered by them and other parties which may not accurately address our specific operating circumstances in California. Holding aside our argument shown above related to the finding of the MAC related to the waste combustion sector, as a company with a significant investment in renewable facilities in this state, Covanta finds value in placing the regulatory imperative on upstream sources of GHGs. This approach excels in its simplicity; it contains an easily discernible number of sources, and it properly focuses on the primary sources of anthropogenic carbon generation. Moreover, an upstream regulatory model would shift the regulatory burden to the level at which compliance costs may be properly configured and allow the carbon price to be reflected in fuel input costs efficiently and effectively such that the costs associated with compliance reach end-users.

[3] As directed in AB 32, the ARB is to review existing and proposed international, federal, and state greenhouse gas emission reporting programs and make reasonable efforts to promote consistency among the programs established pursuant to this part and other programs, and to streamline reporting requirements on greenhouse gas emission sources.

An alternative approach would be one that that would place the primary responsibility for meeting the GHG compliance measures with the load serving entities ("LSE"). We find this approach to be the most economically efficient and from a portfolio management perspective the one easier and more cost-effective to manage. In constructing such a regulatory program, care must be taken to provide contractual and rate remedies that would allow heretofore unanticipated compliance costs to be fully recovered from end-users. As we should have learned from the electrical reregulation process in California, any regulatory program that shields consumers from the real costs of a public policy environmental requirement will not send the requisite market signals necessary for prudent and fair compliance and may have the unintended effect of reducing the reliability of electrical generation in the state.

GHG regulation/compliance at the electric generation sector would result in placing the economic burden on electric generators which have long-term power contracts with utilities in the state. These old contracts do not have provisions for the recovery of compliance cost from the utilities or end-users. In several cases, our contracts are not even linked to any market index that could potentially permit indirect recovery of compliance costs.

GHG Regulatory Compliance and RPS Requirements

Two questions posed by you are of specific interest to Covanta.

22. How would a deliverer/first-seller approach interact with the State's Renewable Portfolio Standard requirements (both existing and proposed)?

This is entirely uncharted territory. RPS facilities are only going to grow in value due to the increasing reliance that is being placed on the sector due to evolving public policy. At the same time, the positive attributes they bring to the carbon debate add a premium to their role in the electricity sector. As a class, their carbon footprints will be expressed in negative terms. Therefore, it is our position that first-sellers of RPS-compliant electricity should be excluded from any GHG regulation under the deliverer/first-seller approach. By definition, these facilities are "renewable" and should not be subject to GHG regulation. Further, as mentioned above, GHG produced by some renewable facilities are (a) insignificant and (b) when the full benefits of specific generation technologies is fairly considered, these facilities should be viewed as net reducers of GHG. Therefore, we believe that GHG regulation directed at the electric generation sector should focus on and should be limited to generators that use fossil fuel for their electricity/energy production, not on renewable energy generators.

23. How should renewable energy generators be treated under a deliverer/first-seller system?

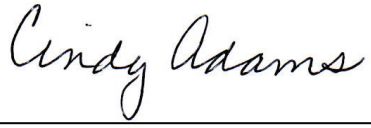
As mentioned in our answer to question 22, all renewable generators in the state should be excluded from any GHG regulation.

Conclusion

Covanta appreciates the opportunity to comment and looks forward to participating further in this proceeding. Please do not hesitate to contact me at 973-822-4144 should you have any questions or comments. Furthermore, Covanta would welcome the opportunity to meet with you to further explain this letter and demonstrate our position.

Dated August 6, 2007, at Fairfield, New Jersey

Respectfully Submitted,



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Proof of Service

I hereby certify that on August 6, 2007, I have served a copy of the COMMENTS OF COVANTA ENERGY CORPORATION ON THE MARKET ADVIORY COMMITTEE REPORT upon all parties listed on the Service List for this proceeding, R-06-04-009. All parties have been served by email or first class mail, in accordance with Commission Rules.

/s/Lisa C. Rodriguez
Lisa C. Rodriguez